

**Letter of Findings: 03-20110360P**  
**Withholding Tax**  
**For the Years 2008-09**

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**ISSUE**

**I. Tax Administration – Failure to Withhold Penalty.**

**Authority:** IC § 6-8.1-10-2.1; [45 IAC 15-11-2](#).

Taxpayer protests the imposition of twenty percent failure to withhold penalties.

**STATEMENT OF FACTS**

Taxpayer is an out-of-state partnership with operations in Indiana. As the result of an audit, the Indiana Department of Revenue ("Department") determined that Taxpayer had not withheld income tax on distributions to its out-of-state shareholders during the tax years 2008 and 2009. However, the out-of-state shareholders had reported and remitted the income on their individual income tax returns for those years. The Department therefore issued proposed assessments for penalties equal to twenty (20) percent of the amount which Taxpayer should have withheld on distributions to its out-of-state shareholders. An administrative hearing was held and this Letter of Findings results. Further facts will be supplied as required.

**I. Tax Administration – Failure to Withhold Penalty.**

**DISCUSSION**

Taxpayer protests the imposition of twenty percent failure to withhold penalties for the tax years 2008 and 2009. Taxpayer states that these were the first two years of its operations in Indiana and that the State did get the appropriate amount of income taxes from the shareholders on their individual returns. Taxpayer has also adjusted its withholding practices to properly withhold on the distributions to its shareholders.

The Department imposed the twenty percent penalties under IC § 6-8.1-10-2.1(h). IC § 6-8.1-10-2.1 provides:

(a) If a person:

- (1) fails to file a return for any of the listed taxes;
- (2) fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment;
- (3) incurs, upon examination by the department, a deficiency that is due to negligence;
- (4) fails to timely remit any tax held in trust for the state; or
- (5) is required to make a payment by electronic funds transfer (as defined in [IC 4-8.1-2-7](#)), overnight courier, or personal delivery and the payment is not received by the department by the due date in funds acceptable to the department; the person is subject to a penalty.

(b) Except as provided in subsection (g), the penalty described in subsection (a) is ten percent (10[percent]) of:

- (1) the full amount of the tax due if the person failed to file the return;
- (2) the amount of the tax not paid, if the person filed the return but failed to pay the full amount of the tax shown on the return;
- (3) the amount of the tax held in trust that is not timely remitted;
- (4) the amount of deficiency as finally determined by the department; or
- (5) the amount of tax due if a person failed to make payment by electronic funds transfer, overnight courier, or personal delivery by the due date.

(c) For purposes of this section, the filing of a substantially blank or unsigned return does not constitute a return.

(d) If a person subject to the penalty imposed under this section can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit tax held in trust, or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall waive the penalty.

(e) A person who wishes to avoid the penalty imposed under this section must make an affirmative showing of all facts alleged as a reasonable cause for the person's failure to file the return, pay the amount of tax shown on the person's return, pay the deficiency, or timely remit tax held in trust, in a written statement containing a declaration that the statement is made under penalty of perjury. The statement must be filed with the return or payment within the time prescribed for protesting departmental assessments. A taxpayer may also avoid the penalty imposed under this section by obtaining a ruling from the department before the end of a particular tax period on the amount of tax due for that tax period.

(f) The department shall adopt rules under [IC 4-22-2](#) to prescribe the circumstances that constitute

reasonable cause and negligence for purposes of this section.

(g) A person who fails to file a return for a listed tax that shows no tax liability for a taxable year, other than an information return (as defined in section 6 of this chapter), on or before the due date of the return shall pay a penalty of ten dollars (\$10) for each day that the return is past due, up to a maximum of two hundred fifty dollars (\$250).

(h) A:

- (1) corporation which otherwise qualifies under [IC 6-3-2-2.8\(2\)](#);
- (2) partnership; or
- (3) trust;

that fails to withhold and pay any amount of tax required to be withheld under [IC 6-3-4-12](#), [IC 6-3-4-13](#), or [IC 6-3-4-15](#) shall pay a penalty equal to twenty percent (20[percent]) of the amount of tax required to be withheld under [IC 6-3-4-12](#), [IC 6-3-4-13](#), or [IC 6-3-4-15](#). This penalty shall be in addition to any penalty imposed by section 6 of this chapter.

(i) Subsections (a) through (c)) do not apply to a motor carrier fuel tax return.

(j) If a partnership or an S corporation fails to include all nonresidential individual partners or nonresidential individual shareholders in a composite return as required by [IC 6-3-4-12\(h\)](#) or [IC 6-3-4-13\(j\)](#), a penalty of five hundred dollars (\$500) per partnership or S corporation is imposed on the partnership or S corporation.

Also, [45 IAC 15-11-2\(b\)](#) provides:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

Finally, [45 IAC 15-11-2\(c\)](#) states in pertinent part:

The department shall waive the negligence penalty imposed under [IC 6-8.1-10-1](#) if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section.

Since the Department imposed the penalties under IC § 6-8.1-10-2.1(h) and since IC § 6-8.1-10-2.1(d) allows waiver of penalty imposed under IC § 6-8.1-10-2.1, waiver of the penalty is allowed if the taxpayer in question can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit tax held in trust, or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect. In this case, Taxpayer provided sufficient documentation and analysis to establish that the failure to withhold on the distributions to its out-of-state shareholders was due to reasonable cause and not due to willful neglect, as required by [45 IAC 15-11-2\(c\)](#)). However, the Department takes this opportunity to remind Taxpayer that any future failure to perform its withholding duties may result in the imposition of these penalties with the likelihood that such a failure will not be considered reasonable.

#### **FINDING**

Taxpayer's protest is sustained.

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